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No. 91-1229

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In the Supreme Court of the United States

OCTOBER TERM, 1992

UNITED STATES OF AMERICA, BY AND THROUGH
INTERNAL REVENUE SERVICE, PETITIONER

v.

BRUCE J. McDERMOTT AND BETTY McDERMOTT
AND ZIONS FIRST NATIONAL BANK, N.A.

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES

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QUESTION PRESENTED

Whether, under Section 6323(a) of the Internal Revenue Code, 26 U.S.C. 6323(a), a judgment lien of a private creditor that predates a federal tax lien has priority over the tax lien with respect to real property interests acquired by the taxpayer after notice of the tax lien was properly filed.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-15a) is reported at 945 F.2d 1475. The opinion of the district court (Pet. App. 16a-24a) is unreported.

JURISDICTION

The judgment of the court of appeals (Pet. App. 25a-26a) was entered on October 2, 1991. On December 19, 1991, Justice White extended the time for filing a petition for a writ of certiorari to and including January 30, 1992. The petition was filed on January 29, 1992, and was granted on May 26, 1992.

The jurisdiction of this Court rests upon 28 U.S.C. 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

Sections 6321 and 6323(a) of the Internal Revenue Code, 26 U.S.C. 6321 and 6323(a), and Section 301.6323(h)-1(g) of the Treasury Regulations on Procedure and Administration, 26 C.F.R. 301.6323(h)-1(g), are set forth at Pet. 2-3.

STATEMENT

1. a. In 1981, Bruce J. and Betty McDermott entered into a contract to sell certain real estate (the "South Street property") that they owned in Salt Lake City, Utah. Upon their entering into the contract of sale, the McDermotts' interest in the property became an interest in personalty under Utah law. The McDermotts retained legal title to the property only as security for payment of the purchase price. On September 23, 1987, after the buyers defaulted on the contract of sale, the McDermotts reacquired the property through foreclosure (Pet. App. 3a-4a, 17a-18a). Upon foreclosure, the McDermotts' interest in the property converted back into a real property interest under state law (*ibid.*).

b. On June 22, 1987, *before* the McDermotts reacquired the South Street property, respondent Zions First National Bank, N.A. (Bank) obtained a state court judgment for \$67,977.67 against the McDermotts. The Bank docketed that judgment in state district court on July 6, 1987 (Pet. App. 2a-3a, 17a-18a).

c. On September 9, 1987, also *before* the McDermotts reacquired the South Street property, the Internal Revenue Service (IRS) filed in the records of

Salt Lake County a notice of federal tax lien in the amount of \$103,657.93. Pursuant to the tax assessment previously made by the Commissioner in December 1986, the notice of lien reflected the McDermotts' unpaid taxes for the years 1977 through 1981 (Pet. App. 2a-4a, 17a-18a).

2. In March 1988, having made a contract to sell the South Street property to a new buyer, the McDermotts sought to obtain releases of the liens on the property (Pet. App. 18a). To permit the sale to occur, the IRS and the Bank entered into an escrow agreement with the McDermotts under which the IRS and the Bank released their claims on the real property but reserved their rights to the cash proceeds of the sale. Under the escrow agreement, the priority of the creditors' claims in the sale proceeds is (Pet. App. 18a-19a n.2):

identical to the priorities of the respective liens [of the parties] as they existed against the real property as of September 23, 1987, after Bruce J. McDermott successfully bid and purchased the property at the Trustee's Sale, notwithstanding the change in form of collateral.

Pursuant to the escrow agreement, the McDermotts instituted this interpleader proceeding in state court by depositing the net proceeds of the sale (\$135,575.50) with the court. The United States then removed the case to federal district court (Pet. App. 2a-3a, 18a).

3. The district court held that the Bank's judgment lien had priority over the federal tax lien in the net proceeds of the sale (Pet. App. 16a-24a). The court acknowledged that, under Utah law, the docketing of the Bank's judgment created a lien in its favor only with respect to real property

in which the McDermotts owned an interest (Pet. App. 19a-20a). The court also recognized that the McDermotts had no real property interest in the South Street property at the time the judgment was docketed because their interest in the existing real estate sales contract was personalty, not realty, under Utah law (*ibid.*). In contrast with the limited character of the Bank's lien under state law, the lien of the United States for unpaid income taxes attaches to "all property and rights to property, whether real or personal, belonging to" the delinquent taxpayer (26 U.S.C. 6321).¹ The district court concluded, however, that the United States had waived its prior right to the proceeds of the McDermotts' "personalty" interest in the first contract of sale for the South Street property by stipulating in the escrow agreement that the parties' priorities are to be determined "as they existed against the real property as of September 23, 1987" (Pet. App. 18a-19a n.2).² The

¹ The federal tax assessment was made on December 9, 1986, and, under 26 U.S.C. 6322, the federal tax lien therefore came into existence on that date. The district court attributed no significance to this fact (Pet. App. 22a n.7).

² In our view, the district court erred in reaching that conclusion, for the escrow agreement also provides that "[n]either party hereto waives any rights, defenses and claims that they may have had * * * in and to the real property, such rights being reserved and shall apply to the cash proceeds being held in escrow in substitution of the subject real property" (Pet. App. 6a). In our view, this case should have been decided in favor of the United States on the ground that its lien attached to the taxpayers' interest in the property before they converted that interest into a real property interest—the only type of interest to which the Bank's lien could have attached (*Cannefax v. Clement*, 818 P.2d 546 (Utah 1991), *aff'g* 786 P.2d 1377, 1380 (Utah Ct. App. 1990);

court therefore considered this case simply as one involving competing liens that attached simultaneously to real property acquired by the McDermotts after the judgment lien and federal tax lien had both been properly placed of record (*id.* at 18a-19a, 21a, 22a).

Viewing the case in this manner, the court concluded that the priority of the competing liens on real property acquired *after* the two liens were filed should be resolved under the rule of "first in time, first in right" (Pet. App. 22a). Because the Bank's judgment had been docketed before notice of the federal tax lien was filed, the court concluded that the judgment lien had priority and therefore must be satisfied in full prior to any distribution to the IRS (*id.* at 22a-23a).

4. The court of appeals affirmed (Pet. App. 1a-15a). While stating that this Court has not addressed the particular situation presented in this case—where a judgment lien and a later-filed tax lien give rise to conflicting claims to after-acquired property—the court of appeals nonetheless interpreted

Butler v. Wilkinson, 740 P.2d 1244, 1254 (Utah 1987)). Under the district court's analysis of the escrow agreement, however, the federal tax lien was not treated as a continuation of its lien against the taxpayers' personality interest in the contract of sale, but as if it had newly attached to the property only as of the time it was converted into a real property interest. The court of appeals accepted the district court's interpretation of the escrow agreement (Pet. App. 6a).

It is, of course, only as a result of the lower courts' interpretation of the escrow agreement that the "after-acquired" property question arises in this case. Since the analysis of the escrow agreement presents narrow issues that lack general importance, however, we have not sought further review of the lower courts' interpretation of that agreement. See Pet. 5-6 n.3.

United States v. Vermont, 377 U.S. 351 (1964), to stand for the proposition that a "non-contingent" lien on all of a person's real property that is "perfected prior to the federal tax lien, will take priority over the federal lien, regardless of whether after-acquired property is involved" (Pet. App. 10a). The court of appeals held that, because the Bank's lien was "non-contingent" (in the sense that the judgment had been properly docketed, was specific in amount, and was applicable to real property owned by the McDermotts), the Bank's lien had priority even with respect to property first acquired by the McDermotts after notice of the federal tax lien had been filed (*id.* at 11a-13a).³

SUMMARY OF ARGUMENT

The federal tax lien arises upon the assessment of taxes and applies to "all property and rights to property, whether real or personal" belonging to the delinquent taxpayer. 26 U.S.C. 6321, 6322. The federal tax lien has priority over the judgment lien of a private creditor unless, before notice of the tax lien is filed, the private lien has been "perfected in the sense that there is nothing more to be done [to establish] the identity of the lienor, the property subject to the lien, and the amount of the lien." *United States v. City of New Britain*, 347 U.S. 81, 84 (1954). Even if the private lien has otherwise been perfected,

³ In so holding, the court of appeals rejected (Pet. App. 13a-14a) the conclusion of the Fifth Circuit in *Southern Rock, Inc. v. B & B Auto Supply*, 711 F. 2d 683 (1983), that, when a private lien and a federal tax lien are filed and perfected in existing property at the same time, the competing lienors are to share the proceeds of the sale of the property in proportion to their claims (Pet. App. 13a-14a).

it acquires no priority over the federal tax lien if the "property subject to the lien" has not been identified, and the lien has not "attached to the property in question," *before* notice of the federal tax lien is filed. *Id.* at 86.

Although the judgment lien involved in this case was filed before notice of the federal tax lien was filed, the taxpayer did not acquire "the property in question" until *after* notice of the federal tax lien was filed. Because the taxpayer did not own the property in question until *after* the notice of tax lien was filed, the judgment lien did not attach to the property until after the tax lien was filed. The federal tax lien therefore has priority under Section 6323(a) of the Internal Revenue Code.

ARGUMENT

UNDER SECTION 6323(a) OF THE INTERNAL REVENUE CODE, THE JUDGMENT LIEN OF A PRIVATE CREDITOR DOES NOT HAVE PRIORITY OVER A FEDERAL TAX LIEN WITH RESPECT TO PROPERTY ACQUIRED BY THE TAXPAYER AFTER NOTICE OF THE FEDERAL TAX LIEN IS FILED

A. The Federal Tax Lien Has Priority Over A Prior-Filed Judgment Lien With Respect To Property Acquired By The Taxpayer After Notice Of The Tax Lien Is Filed

1. Section 6321 of the Internal Revenue Code establishes "a lien in favor of the United States upon all property and rights to property, whether real or personal" belonging to a taxpayer who, after demand, "neglects or refuses to pay" taxes owed to the United States. 26 U.S.C. 6321. Under Section 6322 of the Code, this broad federal lien arises "at the time the assessment is made" and continues until the taxes are paid or the lien becomes unenforceable by passage

of time. 26 U.S.C. 6322.⁴ The federal tax lien attaches to all property owned by the debtor at the time the lien arises, and also to all other property thereafter acquired by the taxpayer. *Glass City Bank v. United States*, 326 U.S. 265, 268 (1945) ("the lien applies to property owned by the delinquent at any time during the life of the lien"); *Graves v. Commissioner*, 12 B.T.A. 124, 133 (1928) (the federal tax lien applies "of course, to all the property that the tax debtor subsequently acquires").

Sections 6321 and 6322 of the Code originated with the Act of July 13, 1866, ch. 184, § 9, 14 Stat. 107.⁵ The provisions of that Act did not indicate whether the federal tax lien takes priority over claims of other creditors asserted in the same property. In *United States v. Snyder*, 149 U.S. 210 (1893), however, this Court held that the federal tax lien that arises upon assessment has priority in all of the taxpayer's property even without notice to other creditors, and even over the rights of a subsequent bona fide purchaser for value who took without notice of

⁴ Section 6322 of the Internal Revenue Code provides that, "[u]nless another date is specifically fixed by law, the lien imposed by section 6321 shall arise at the time the assessment is made and shall continue until the liability for the amount so assessed (or a judgment against the taxpayer arising out of such liability) is satisfied or becomes unenforceable by reason of lapse of time." 26 U.S.C. 6322.

⁵ The relevant text of that statute was as follows: "And if any person, bank, association, company, or corporation, liable to pay any tax, shall neglect or refuse to pay the same after demand, the amount shall be a lien in favor of the United States from the time it was due until paid, with the interest, penalties, and costs that may accrue in addition thereto, upon all property and rights to property belonging to such person, bank, association, company, or corporation." § 9, 14 Stat. 107.

the lien. *Id.* at 213-214. Sections 6321 and 6322 have not been altered in any material respect since *Snyder* and therefore incorporate this broad principle.

While the general principle established in *Snyder* thus remains effective, it has been limited somewhat by a variety of provisions enacted by Congress (now set forth in Section 6323 of the Code) that subordinate the federal tax lien to the claims of other creditors in specific, carefully delineated circumstances. The present case concerns the provisions of Section 6323(a), which had its origin in the Act of Mar. 4, 1913, ch. 166, § 3186, 37 Stat. 1016. The 1913 Act was enacted specifically to limit the potential harshness of the *Snyder* decision in three narrow situations. See H.R. Rep. No. 1018, 62d Cong., 2d Sess. 2 (1912). The 1913 Act accepted the general rule of *Snyder*, but modified it in part by providing that the federal tax "lien shall not be valid as against any mortgagee, purchaser or judgment creditor until notice of such lien shall be filed." § 3186, 37 Stat. 1016. With only slight changes in phrasing, this provision has been carried forward to Section 6323 (a) of the current Code.⁶

In its current form, Section 6323(a) provides that the federal tax lien "shall not be valid as against any purchaser, holder of a security interest, mechanic's

⁶ The extensive changes to Section 6323 that were enacted by Congress in 1966 are discussed at pages 15-18, *infra*. These changes did not alter the scope of the priority afforded the federal tax lien under Section 6323(a), but added numerous additional protective provisions for private creditors in Section 6323(c)-(h). Although the changes enacted in 1966 are not directly relevant to the question presented in this case, they confirm that the tax lien has priority over prior-filed judgment liens with respect to property acquired after notice of the tax lien is filed. See pages 15-18, *infra*.

lienor, or judgment lien creditor until notice" of the federal tax lien has been properly filed in local property records.⁷ 26 U.S.C. 6323(a). The origin and history of the federal tax lien provisions reflect a studied intent by Congress to exclude from the effect of the federal tax lien *only* those third-party "interests which [Congress] specifically included in [Section 6323] and no others." *United States v. Security Trust & Savings Bank*, 340 U.S. 47, 53 (1950) (Jackson, J., concurring) (emphasis added). Accord, *United States v. City of New Britain*, 347 U.S. 81, 88 (1954); *United States v. Gilbert Associates, Inc.*, 345 U.S. 361, 364 (1953); 14 J. Mertens, *The Law of Federal Income Taxation* § 54A.03, at 15-16 (1991).

Under Section 6323(a), when a private lien of the type described in that Section has been "perfected" in the taxpayer's property *before* notice of the federal tax lien is filed, the private lien is entitled to priority with respect to that property under the general rule that "the first in time is the first in right." *United States v. City of New Britain*, 347 U.S. at 85. For the private lien to be perfected in the taxpayer's property, and thereby obtain priority over a later-filed tax lien, the lien must be certain and specific as to the identity of the lienor, the amount of the lien, and the collateral or property to which it applies. *Id.* at 84.⁸ To obtain priority over the federal tax

⁷ The filing procedures to be followed by the Internal Revenue Service in giving notice of the federal tax lien are set forth in Section 6323(f) of the Code. See 26 U.S.C. 6323(f). It is not disputed that these statutory procedures were followed in this case and that notice of the federal tax lien was properly filed.

⁸ The Court has referred to these requirements in distinguishing between liens that are "choate" and "inchoate." To

lien under Section 6323(a), the private lien must be (*United States v. City of New Britain*, 347 U.S. at 84):

perfected in the sense that there is nothing more to be done [to establish] the identity of the lienor, the property subject to the lien, and the amount of the lien * * *.

See also *United States v. Pioneer American Ins. Co.*, 374 U.S. at 89. Whether the private lien is "sufficiently specific and perfected" prior to the date of notice of the tax lien, and thus obtains priority under Section 6323(a), is a question of federal law, not state law. *United States v. Waddill, Holland & Flinn, Inc.*, 323 U.S. 353, 356-357 (1945). See also *United States v. Pioneer American Ins. Co.*, 374 U.S. at 88 ("it is a matter of federal law when such a lien has acquired sufficient substance and has become so perfected as to defeat a later-arising or later-filed federal tax lien").

Even if the private lien has otherwise been perfected, it acquires no priority over the federal tax lien if the "property subject to the lien" has not been

be perfected against a federal tax lien, the private judgment lien must have "attached to the property in question and bec[o]me choate" before notice of the federal tax lien is filed. *United States v. Pioneer American Ins. Co.*, 374 U.S. 84, 88 (1963) (quoting *United States v. City of New Britain*, 347 U.S. at 86). The Court has invoked and applied these requirements frequently. See, e.g., *United States v. Acri*, 348 U.S. 211 (1955); *United States v. Liverpool & London & Globe Ins. Co.*, 348 U.S. 215 (1955); *United States v. Scovil*, 348 U.S. 218 (1955); *Aquilino v. United States*, 363 U.S. 509 (1960); *United States v. Durham Lumber Co.*, 363 U.S. 522 (1960); *United States v. Vermont*, 377 U.S. 351, 357 (1964); *United States v. Equitable Life Assurance Society*, 384 U.S. 323 (1966).

identified, and the lien has not "attached to the property in question," before notice of the federal tax lien is filed. *United States v. City of New Britain*, 347 U.S. at 86. See also *United States v. Equitable Life Assurance Society*, 384 U.S. 323, 328 (1966); *Illinois v. Campbell*, 329 U.S. 362, 373 (1946). When the "property subject to the lien" has not been identified and the lien has not "attached to the property in question" before notice of the federal tax lien is filed, the private lienor has only the hope "of a more perfect lien to come" (*United States v. Security Trust & Savings Bank*, 340 U.S. at 50 (quoting *New York v. Maclay*, 288 U.S. 290, 294 (1933))).⁹ That hope is not sufficient to defeat the federal lien.

The requirements (i) that the private lien be fully perfected, (ii) that it identify the property subject to the lien, and (iii) that it attach to the property before notice of the federal tax lien is filed are federal rules adopted by this Court to implement the priorities established by the federal tax lien provisions. *United States v. Pioneer American Ins. Co.*, 374 U.S. at 88. These federal rules, however, are consistent with ordinary commercial law principles. For example, under Section 9-303(1) of the Uniform Commercial Code, a security interest is not perfected until "it has attached" to the property involved. Section 9-203(1)(c) of the Uniform Commercial Code specifies that a security interest in property cannot attach until "the debtor has rights in the collateral." Before the debtor has acquired rights in the property, and the private lien has attached to the property, the

⁹ As the Ninth Circuit put it in *United States v. J.D. Granger Co.*, 945 F.2d 259 (1991), the property to which the lien applies must be "definite, and not merely ascertainable in the future." *Id.* at 263.

private lien would not be "enforceable against the debtor or third parties with respect to the collateral" under normal commercial law concepts (U.C.C. § 9-203(1)).

Accordingly, when the taxpayer first acquires ownership of property *after* notice of the federal lien is filed, it is the tax lien, rather than the private lien, that has priority under Section 6323(a).¹⁰ See *United States v. City of New Britain*, 347 U.S. at 86 (the priority of the private lien "must depend on the time it attached to the property in question"); *United States v. Equitable Life Assurance Society*, 384 U.S. at 328 (same); *Don King Productions, Inc. v. Thomas*, 945 F.2d 529, 534 (2d Cir. 1991). Even when "the identity of the [private] lienor was known and the amount of the [private] lien was established," the federal tax lien has priority if "the property subject to the lien was not in existence at the

¹⁰ The one historical exception to this conclusion was for purchase money mortgages. If property is acquired with a purchase money mortgage *after* notice of a tax lien is filed, the mortgage has priority even though the taxpayer had no rights in the property at the time the tax lien was filed. The special treatment afforded to purchase money mortgages is "based upon the concept that the taxpayer has acquired property or a right to property [to which the lien created by Section 6321 may apply] *only to the extent* that the value of the whole property or right exceeds the amount of the purchase money mortgage." H.R. Rep. No. 1884, 89th Cong., 2d Sess. 4 (1966) (emphasis added). See *Allan v. Diamond T Motor Car Co.*, 291 F.2d 115 (10th Cir. 1961); Coogan, *The Effect of the Federal Tax Lien Act of 1966 Upon Security Interests Created Under the Uniform Commercial Code*, 81 Harv. L. Rev. 1369, 1374 & n.23 (1968). The Internal Revenue Service has acquiesced in this treatment of purchase money mortgages. See Rev. Rul. 68-57, 1968-1 C.B. 553.

time the government's lien arose." *Ibid.*¹¹ When the taxpayer acquires rights in the property *after* notice of the federal tax lien is filed, the tax lien and the prior-filed private lien "attach to the [after-acquired property] at the same instant" (Coogan, *The Effect of the Federal Tax Lien Act of 1966 Upon Security Interests Created Under the Uniform Commercial Code*, 81 Harv. L. Rev. 1369, 1383-1384 (1968)). Since the private lien is not perfected until it attaches to the property, and is thus not perfected with respect to after-acquired property *before* notice of the tax lien is filed, "the tax lien takes priority" over the private lien under the express terms of Section 6323(a). Coogan, *supra*, 81 Harv. L. Rev. at 1383-1384. See also *Texas Oil & Gas Corp. v. United States*, 466 F.2d 1040, 1052-1054 (5th Cir. 1972); *MDC Leasing Corp. v. New York Property Ins. Underwriting Ass'n*, 450 F. Supp. 179, 181 (S.D.N.Y. 1978), *aff'd* without published opinion, 603 F.2d 213 (2d Cir. 1979) (Table); *United States v. Graham*, 96 F. Supp. 318, 321 (S.D. Cal. 1951), *aff'd sub nom. California v. United States*, 195 F.2d 530 (9th Cir. 1952), *cert. denied*, 344 U.S. 831 (1952); *Gaeta v. United States*, 50 A.F.T.R. 2d 5509 (W.D.N.Y. 1982); *Iowa Fair Plan v. United States*, 257 N.W. 2d 626, 629-630 (Iowa 1977).¹²

¹¹ See also Coogan, *supra*, 81 Harv. L. Rev. at 1377, 1384. There can be no "security interest in property if the debtor at the time of its purported creation has no rights therein. * * * [When the security interest and the later-filed tax lien] attach to the [after-acquired property] at the same instant, * * * the tax lien takes priority over the security interest" with respect to that property. *Id.* at 1383-1384.

¹² In *Southern Rock, Inc. v. B & B Auto Supply*, 711 F.2d 683, 688-689 (1983), the Fifth Circuit concluded that, in the unusual factual scenario where the private lien and notice

2. The structure and history of the Federal Tax Lien Act of 1966 (Pub. L. No. 89-719, § 101, 80 Stat. 1125) confirm that the federal tax lien has priority in property acquired by the taxpayer after notice of the federal lien is filed. In that Act, Congress confirmed the basic "assumption that the general tax lien outranks all competing interests" but adopted several new categories of private interests to be given priority over the federal tax lien in carefully designated situations. Young, *Priority of the Federal Tax Lien*, 34 U. Chi. L. Rev. 723, 724 (1967).¹³ These new categories of protected commer-

of the federal tax lien are filed simultaneously, the liens share pro rata in the proceeds of the taxpayer's property. That conclusion disregards the language of Section 6323(a). "[U]ntil notice" of the federal tax lien is filed, the statute provides protection for specific types of perfected private liens. 26 U.S.C. 6323(a). If the private lien is not perfected "until notice" of the federal lien is filed, it is not protected by the statute. A private lien perfected at the same instant that notice of the federal lien is filed is not protected under Section 6323(a) because the federal lien has "priority," not "parity," when the private lien is not perfected first. *Texas Oil & Gas Corp. v. United States*, 466 F.2d at 1047, 1052; see *MDC Leasing v. New York Property Insurance Underwriting Ass'n*, 450 F.Supp. at 181.

In any event, the unusual situation presented in *Southern Rock* does not exist in this case. This case does not involve the priorities in *existing* property that result from the simultaneous filing of a perfected private lien and notice of the federal tax lien. Instead, this case concerns a prior-filed private lien that was *not* perfected in the property right at issue, because the property right at issue *did not exist*, until *after* notice of the federal tax lien was filed.

¹³ "The amended tax lien law starts, as the old one did, with an assumption that the general tax lien outranks all competing interests. The 1966 Act made no change in section 6321, which creates a lien in favor of the United States for the amount of tax, together with incidentals, that anyone has

cial interests are set forth, and described in detail, in Section 6323(c)-(h) of the Code. 26 U.S.C. 6323(c)-(h). Although these new provisions are not directly applicable to the priority afforded a judgment lien creditor—which was not altered in the 1966 Act—they nonetheless reveal Congress's clear acceptance of the established rule that the federal tax lien has priority in property acquired by a taxpayer *after* notice of the federal tax lien has been filed.

For example, in amending Section 6323(a), Congress provided a priority for a "security interest" that comes into existence before notice of the federal tax lien is filed. 26 U.S.C. 6323(a). Congress provided, however, that a "security interests exists" for purposes of this provision only "at such time as the property is in existence" (26 U.S.C. 6323(h)(1)). By requiring that the property subject to the security interest be "in existence" for the security interest to be perfected against the unfiled tax lien, Congress applied the ordinary commercial rules of "attachment"¹⁴ and recognized that "there can be no UCC security interest in property if the debtor at the time of its purported creation has no rights therein." Coogan, *supra*, 81 Harv. L. Rev. at 1383.¹⁵ The

'neglected' to pay, upon all his property and rights to property. Chiefly, section 6323 is an elaborate set of qualifications on the assumption that such lien is good against all comers." Young, *supra*, 34 U. Chi. L. Rev. at 724.

¹⁴ The Federal Tax Lien Act of 1966 represents "in part an attempt to conform the lien provisions of the internal revenue laws to the concepts developed in [the] Uniform Commercial Code." H.R. Rep. No. 1884, *supra*, at 1-2.

¹⁵ The federal requirement that "the property [be] in existence" for the private security interest to prime the unfiled tax lien under Section 6323(h)(1) applies "even though local law may relate a security interest back to an earlier date and even

House Report on the Federal Tax Lien Act of 1966 thus states specifically that a prior-filed security interest does *not* have priority over the federal tax lien with respect to "assets acquired after the tax lien filing." H.R. Rep. No. 1884, 89th Cong., 2d Sess. 8 (1966).

When a security interest attaches to property acquired *after* notice of the federal tax lien is filed, the federal tax lien thus has priority under Section 6323(a). See 26 U.S.C. 6323(h)(1); H.R. Rep. No. 1884, *supra*, at 8. In this situation, however, the security interest may nonetheless "be protected in accordance with the provisions of new subsections (c) and (d)." H.R. Rep. No. 1884, *supra*, at 35. Section 6323(c) protects certain types of "commercial transaction" security interests (which do not include judgment liens) that "came into existence after tax lien filing," but only if such interests arise under "the terms of a written agreement entered into before tax lien filing" (26 U.S.C. 6323(c)(1)). If the theory of the court of appeals in this case were accepted—and a prior-filed private lien were given priority over the tax lien with respect to property acquired "after tax lien filing"—it would have been unnecessary for Congress to enact the special commercial financing provisions of Section 6323(c) and (d). By enacting the carefully limited exceptions for special types of commercial financing agreements, however, Congress clearly did *not* alter the general rule that the federal lien has priority in property "acquired after the tax lien filing." H.R. Rep. No.

though it might be an effective security interest as of the earlier date under the Uniform Commercial Code." H.R. Rep. No. 1884, *supra*, at 11-12.

1884, *supra*, at 8.¹⁶ That general rule controls this case.

B. This Court's Decision in *United States v. Vermont* Does Not Alter The General Rule That The Federal Tax Lien Has Priority In Property Acquired by The Taxpayer After Notice of The Tax Lien Is Filed

For a private lien to be perfected against the federal tax lien under Section 6323(a), the private lien must have "attached to the property in question" (*United States v. City of New Britain*, 347 U.S. at 86) before notice of the federal tax lien is filed. The court of appeals erred in concluding (Pet. App. 10a-12a) that this Court's decision in *United States v. Vermont*, 377 U.S. 351 (1964), requires a different result.

The *Vermont* case did not concern the question of when a private lien attaches to the taxpayer's property and becomes perfected against the federal tax lien. Instead, *Vermont* concerned the different question whether a state tax lien that applies to "all" the debtor's property was "sufficiently specific" to encompass the debtor's bank accounts as "property subject to the lien," as required by *United States v. Waddill, Holland & Flinn, Inc.*, 323 U.S. at 356, and *United States v. City of New Britain*, 347 U.S. at 84. In *Vermont*, the Court held that the word "all" sufficiently described the property owned by the debtor to which the lien applied and therefore satisfied the standard of specificity required by *Waddill* and *City of New Britain*. See 377 U.S. at 358. The Court in

¹⁶ See Coogan, *supra*, 81 Harv. L. Rev. at 1414 ("For protection as to collateral added * * * after tax lien filing, [the secured party] must fit his transaction into one of the categories of subsection (c) or qualify for a purchase money interest under case law."). See also note 10, *supra*.

Vermont did not hold that the State's lien could have attached to, and thus been perfected in, *property that the taxpayer did not own before the federal tax lien was filed*. The Court neither addressed nor abandoned the general rule that, for the private lien to be perfected against the federal tax lien, it must have "attached to the property in question" before notice of the tax lien is filed. Nor did the Court abandon the settled rule that the property must exist, and the taxpayer must have rights in it, before the private lien may attach to the property and become perfected against the unfiled federal tax lien. See H.R. Rep. No. 1884, *supra*, at 8; pages 7-17, *supra*.

C. The Property At Issue In This Case Was Not Acquired By The Taxpayer Until After Notice Of The Federal Tax Lien Was Filed

When the Bank docketed its judgment against the McDermotts on July 6, 1987, it gained no lien upon *any* property. As the lower courts acknowledged, the Utah statute (Utah Code Ann. § 78-22-1 (1992)) creates a lien only upon real property of the judgment debtor (Pet. App. 2a, 20a), and the land contract by which the McDermotts in 1981 sold the South Street property left them with an interest that Utah law classified as personalty (*id.* at 6a n.5, 19a-20a). See *Cannefax v. Clement*, 818 P.2d 546 (Utah 1991), *aff'g* 786 P.2d 1377, 1380 (Utah Ct. App. 1990). It was only when the McDermotts foreclosed the defaulted land contract and reacquired the South Street property on September 23, 1987, that a lien upon that property in favor of the Bank came into existence.¹⁷ Pet. App. 2a-3a, 21a.

¹⁷ Federal law, of course, "determines the priority of competing liens asserted against the taxpayer's 'property' or

Meanwhile, when the Internal Revenue Service assessed unpaid federal income taxes against the McDermotts in December 1986, the United States gained a lien for the amount of the unpaid taxes, and interest, "upon all property and rights to property, whether real or personal, belonging to such [taxpayers]." 26 U.S.C. 6321. And, when the United States filed notice of the federal tax lien with the Salt Lake County Recorder on September 9, 1987, it made that lien invulnerable to the claim of any subsequent "purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor" under Section 6323(a) of the Code. 26 U.S.C. 6323(a); see Pet. App. 2a, 17a. As matters then stood, the United States had a mature and perfected lien upon the interest of the McDermotts in the South Street property, and the Bank had no lien—or a lien upon nothing.¹⁸ So matters stood until September 23, 1987, when the McDermotts reacquired the South Street

'rights' to 'property.'" *Aquilino v. United States*, 363 U.S. 509, 514 (1960). It is well established as a matter of federal law that the doctrine of relation back may not be applied to perfect a private lien that was not perfected at the time notice of the tax lien is filed. See *United States v. Pioneer American Ins. Co.*, 374 U.S. at 92 n.11; *United States v. Security Trust & Savings Bank*, 340 U.S. at 50. See also note 15, *supra*.

¹⁸ Prior to foreclosure on September 23, 1987, the defaulting purchaser's interest in the real estate was not subject to the Bank's judgment lien against the McDermotts. See page 19, *supra*. The purchaser could have sold the property—and thereby satisfied their sale contract with the McDermotts—free of any claim by the Bank. But, if such a sale had occurred, the McDermotts' interest in the proceeds of the sale would have been subject to the federal lien under Section 6321 of the Code. See 26 U.S.C. 6321 (tax lien applies to "all property and rights to property, whether real or personal").

property by foreclosure, and thereby gained real property to which the Bank's judgment lien could attach.¹⁹

The courts below erred in holding that, even though the lien of the Bank did not attach to the reacquired property until *after* notice of the tax lien had been filed, the Bank's lien was entitled to priority on the basis, as the district court held (Pet. App. 21a-24a), of the rule of "first in time, first in right", or, as the court of appeals held (*id.* at 7a-13a), because "creditors who perfect their liens before the filing of a federal tax lien have priority" (*id.* at 13a). The Bank's lien was not "first in time," nor was it "perfected before the filing of a federal tax lien," because the Bank's lien had not "attached to the property in question" (*United States v. City of New Britain*, 347 U.S. at 86) before notice of the tax lien was filed.

Before the McDermotts reacquired the South Street property, the Bank had the mere hope "of a more perfect lien to come" (*United States v. Security Trust & Savings Bank*, 340 U.S. at 50 (quoting *New York v. Maclay*, 288 U.S. at 294)). Since the Bank's lien in the South Street property did not attach to that

¹⁹ The district court read the escrow agreement to waive the priority of the United States based upon its lien upon the McDermotts' interest in the land contract, so that, when the McDermotts reacquired the property, "the liens of the competing claimants simultaneously attached as against the merged interests in real property" (Pet. App. 21a).—The court of appeals agreed with this interpretation of the escrow agreement (*Id.* at 6a). Even if that proposition is accepted (see note 2, *supra*), there is no doubt that the federal lien could and did attach to the taxpayer's real property interest in the South Street property when reacquired by the McDermotts. See *Glass City Bank v. United States*, 326 U.S. 265 (1945).

property until *after* notice of the tax lien was filed, the tax lien has priority under Section 6323(a).

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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